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SUBJECT: SOUTH AFRICA ECONOMIC NEWSLETTER May 20 2005 ISSUE

¶1. Summary. Each week, AmEmbassy Pretoria publishes an economic newsletter based on South African press reports. Comments and analysis do not necessarily reflect the opinion of the U.S. Government. Topics of this week's newsletter are:

- ANC to Discuss Relaxation in SA's Labor Market;
- Empowerment Funding Structure Debated;
- Savings Still Low Although Conditions Improved;
- SA Productivity Drives Increase in Global Competitiveness;
- Manufacturing and Retail Sales Show Signs of Slowdown;
- Sub-Saharan African Transport Expensive; and
- 2004/05 Budget Deficit Lower.

End Summary.

ANC TO DISCUSS RELAXATION IN SA'S LABOR MARKET

¶2. In preparation for the African National Congress' (ANC) general council meeting in June, a plan calling for a dual labor market, where young workers would earn less and their employers might not meet all the current labor regulations, is circulating. The plan is part of a search for solutions to South Africa's high unemployment. Acknowledging that young people constitute 60 percent of South Africa's unemployed, the ANC document says that subjecting young people to a more flexible labor relations regime would mean waiving the minimum wage and other collective bargaining arrangements (including limits on overtime work) and make it easier to dismiss poor workers. Another proposal is that industrial development zones be free of labor laws such as the Labor Relations Act and Basic Conditions of Employment Act, encouraging investment and employment growth in poorer provinces such as Eastern Cape and KwaZulu-Natal. Initial reactions from trade unions were negative with the Congress of South African Trade Unions (COSATU) opposing attempts by government to "reverse worker rights." Any change to existing labor laws would be unconstitutional. Officially, COSATU and the South African Communist Party would not comment on the proposals, saying they had not yet seen the document. The proposal also suggests changing the definition of small business, increasing its size from 50 to 200 employees and exempting it from parts of existing labor laws. Source: Business Day, May 16.

EMPOWERMENT FUNDING STRUCTURE DEBATED

¶3. A discussion document for the African National Congress (ANC) national general council meeting criticizes the current way of funding empowerment deals. Currently most deals are debt-driven. Since the money spent is not invested productively, these deals represent a drain on the economy. The deals, based on debt-financing, are unsustainable. Other critics say large empowerment deals are structured in so that they are unprofitable for long periods of time. Another problem is that empowerment partners do not have money for financing proposed transactions. Some argue for more flexibility in the funding arrangements of empowerment deals to allow for an early exit. John Kane-Berman, Chief Executive of the South African Institute of Race Relations, says the fundamental problem is that there are not enough black people to purchase large amounts of shares. He suggests that attracting foreign direct investment and combating unemployment should be government's primary concerns. He also argues that few empowerment deals generate business; they just transfer assets. Source: Business Day, May 17.

SAVINGS STILL LOW ALTHOUGH CONDITIONS IMPROVED

¶4. South Africans continue to spend their surplus cash rather than save it, despite the excellent environment. The South African Savings Institute's (SASI) national savings barometer for the fourth quarter of 2004 shows that the environment for saving improved by 1.98 index points to 115.06 in December. This was the fifth quarter

in a row that conditions improved. Despite the improvement, gross savings as a percentage of gross domestic product (GDP) fell from 15 percent in the third quarter 2004 to 13.5 percent in December. The lower savings ratio was mainly attributable to the corporate and household sectors, with the government sector's ratio practically unchanged. SASI noted that an increase in business confidence, lower producer inflation figures and low interest rates have led to an improvement in savings conditions for businesses and increases in disposable income improved the savings environment for consumers. Lower government spending as a percentage of GDP and the decrease in government debt as a proportion of GDP were among the factors contributing to the improvement in government's saving environment in the last quarter of ¶2004. Source: Business Day, May 16.

SA PRODUCTIVITY DRIVES INCREASE IN GLOBAL COMPETITIVENESS
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¶5. According to the National Productivity Institute (NPI), South Africa's rising productivity, growing at more than 3 percent per year since 1996, forms the basis for South Africa's improved international competitiveness. South Africa improved its ranking from 49 to 46 out of 60 countries according to the latest World Competitiveness Report compiled by the Swiss-based Institute for Management Development, primarily due to due an improved 2004 economic performance. Despite this improvement in its rankings, South Africa showed a decline in three of the four ranking categories since 2004. Apart from a sharp improvement in economic performance, areas such as business efficiency, government efficiency and infrastructure development had actually declined in comparison with other countries. The NPI said business efficiency was hampered by inadequate skilled labor, the brain drain, low employment rate, insufficient finance skills, and shortages of competent senior managers and entrepreneurs. South African employers were also not keeping pace with other countries in terms of planning and supervision of employees. Source: Business Day, May 16.

MANUFACTURING AND RETAIL SALES SHOW SIGNS OF SLOWDOWN
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¶6. According to Statistics SA, manufacturing production grew by 1.2 percent (y/y) and 0.9 percent growth (m/m) in March, continuing its fourth month of slower growth. On a quarterly basis, six out of 10 manufacturing sub-sectors reported a decline in output in the period ending in March 2005, with basic iron and steel and machinery contributing most to manufacturing production decline. The strong rand, slower growth in the Euro zone economies, and higher oil prices are manufacturers' key concerns. Retail sales also slowed in the first two months of 2005 compared to December 2004's growth of 10.2 percent (y/y). In January 2005, real retail sales increased by 3.4 percent (y/y), showing a monthly decline of 32.6 percent. February's y/y growth was 5.4 percent, while monthly growth (-1.5 percent) again declined but at a much slower rate. The April 14th 50 basis point reduction in interest rates should support additional positive growth in retail sales, although sales of motor vehicles show signs of deceleration. Source: Business Day, May 13; Standard Bank, Taking Stock and Manufacturing Unpacked.

SUB-SAHARAN AFRICAN TRANSPORT EXPENSIVE

¶7. Despite the sub-Saharan Africa region owning the largest transport infrastructure in Africa, it had the highest transport costs on the continent. Sub-Saharan Africa owns 83 percent of all African railways, but transport costs as a proportion of import value in the region were about 16 percent, compared with an average of 13 percent in other African countries, according to Minister of Transport Jeff Radebe. Transport costs in Africa were considerably higher than the 9 percent average in other developing countries and more than double the world average. North Africa had the lowest freight costs on the continent, while West Africa was slightly lower than the sub-Saharan region at 14 percent. High transport costs are a big concern in South Africa. The country owns 42 percent of the sub-Saharan railway infrastructure, but transport costs come in at about 13 percent of gross domestic product. Maria Ramos, the Chief Executive of Transnet (a state-owned transportation enterprise) said that the transport utility wants to lower transport costs to between 7 percent and 8 percent. Radebe said South Africa had the biggest rolling stock on the continent, accounting for about 47 percent of the locomotives in sub-Saharan Africa, 32 percent of locomotives in Africa, 62 percent of freight wagons and carries 71 percent of the continent's rail freight and 91 percent of sub-Saharan Africa's. Source: Business Report, May 17.

2004/05 BUDGET DEFICIT LOWER

¶8. National Treasury stated that South Africa's national budget deficit for the financial year 2004-05 narrowed to 1.5 percent of gross domestic product (GDP), compared to a April estimate of 1.6 percent and a February estimate of 2.3 percent. The consolidated deficit, which covers both national and provincial expenditures, is now projected at 1.3 percent compared to February's estimate of 2.5 percent. In April, the lower than expected deficit was due to almost R10 billion ($1.5 billion, at R6.4 per dollar) surplus revenue collected by the South African Revenue Service. Better than expected economic growth, led by strong consumer spending, resulted in higher collected tax revenues. Acknowledging concerns about the provinces' capabilities of delivering basic services quickly, National Treasury stated that the reduced deficit should not be viewed as under spending as it represented savings, higher tax collections and the non-transfer of funds. Spending by national and provincial governments was 97.8 percent of their consolidated adjusted budgets in 2004/05. These figures would be revised when national and provincial departments had finalized and reconciled financial statements for submission to the auditor-general by May 31. Source: Business Day and Business Report, May ¶18.

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